SUPREME COURT, U. S.

Supreme Court of the United States

October Term, 1973

No. 73-890

ERIE LACKAWANNA RAILWAY COMPANY, Debtor,
Petitioner,

vs.

NORFOLK AND WESTERN RAILWAY COMPANY,
Respondent.

PETITION FOR A WRIT OF CERTIORARI
To the United States Court of Appeals
For the Sixth Circuit

SHERMAN DYE
RICHARD KATCHER
1956 Union Commerce Building
Cleveland, Ohio 44115
Counsel for Petitioner

THE GATES LEGAL PUBLISHING CO., CLEVELAND, OHIO—TEL. (216) 621-5647

INDEX

Opinions Below 1
Jurisdiction 2
Questions Presented 2
Statutes and Regulations Involved 3
Statement of Case 3
Reasons for Granting the Writ of Certiorari 6

1. Whether Tax Attributes Constitute "Property" for Bankruptcy Purposes Is an Issue of Crucial Significance in Bankruptcy Administration 6

   a. Tax Attributes Such As Losses and Investment Credits Are Property of Substantial Value That Can Be Realized Upon for the Benefit of Creditors 6

   b. Tax Attributes Are Property Within the Meaning of Section 77(a) of the Bankruptcy Act 9

   c. It Is of Crucial Significance to the Northeast Railroads in Reorganization That Their Tax Attributes Fall Within the Meaning of Property 10

   d. The Scope of Property with Reference to Tax Attributes Is a Recurring Problem in Bankruptcy Administration and a Conflict Exists in the Circuit Courts of Appeal As to Whether Tax Refunds Arising from Withholding Taxes Is Such Property 11

2. Whether the District Court in Fulfilling Its Duty to Protect the Property of the Debtor, In-

cluding Its Tax Attributes, Can Direct the Parent As to What Tax Elections Are to Be Made in a Consolidated Return Which Affect the Debtor's Property Is a Novel and Important Issue in the Administration of the Consolidated Returns Regulations 13

Conclusion 18

Appendix:

Opinion and Order of the District Court A1
Order of the Court of Appeals A14
Bankruptcy Act, 11 U.S.C. §205 ..... A18
Internal Revenue Code of 1954, 26 U.S.C. §1502 ..... A19
Treasury Regulations, 26 CFR §1.1502-77 ..... A19

CITATIONS

Cases

Aveni, In re, 458 F.2d 972 (6th Cir. 1972), *cert. denied*, 409 U.S. 877 (1972) 12

Boston & Maine Railroad, In the Matter of, Report and Order of Administrative Law Judge, I.C.C., Finance Docket No. 26115 11

Case v. New York Central Railroad Company, 204 N.E.2d 643 (N.Y. Ct. App. 1965) 10

Cedor, In re, 337 F. Supp. 1103 (N.D. Cal. 1972), *aff'd per curiam*, 470 F.2d 996 (9th Cir. 1972) 12

Jones, In re, 337 F. Supp. 620 (D.C. Minn. 1971), *leave to appeal denied* (8th Cir. May 14, 1971), *cert. denied*, 404 U.S. 1040 (1972) 12

Kingswood, In re, 343 F. Supp. 498 (C.D. Cal. 1972), *rev'd per curiam*, 470 F.2d 996 (9th Cir. 1973), petition for cert. filed August 13, 1973 (No. 73-289) 12

Kokoszka, In re, 479 F.2d 990 (2nd Cir. 1973) 12

Lehigh Railroad Company, In the Matter of, (E.D. Pa. Bankruptcy No. 70-432) 11

Lines v. Frederick, 400 U.S. 18 (1970) 12

New Haven Inclusion Cases, 399 U.S. 392 (1970) 9

Penn-Central Merger and N & W Inclusion Cases, 389 U.S. 486 (1968) 4

Richards Chrysler-Plymouth Corp., Inc., In re Bob, 473 F.2d 262 (2nd Cir. 1973), *cert. denied*, May 29, 1973 ..... 9, 15

Segal v. Rochelle, 382 U.S. 375 (1966) 6, 9, 15, 16

Western Pacific Railroad Corp. v. Western Pacific Railroad Co., 345 U.S. 247 (1952) 7

Statutes

Bankruptcy Act:

§70a(5) (11 U.S.C. §110a) 7, 12
§77(a) (11 U.S.C. §205) 2, 3, 9, 12, 16

Internal Revenue Code of 1954 (26 U.S.C.):

§172(b) 10
§1502 3
§6012(b)(3) 9

United States Code:

28 U.S.C. §1254(1) 2

Miscellaneous

Annual Report (1972), Bomaine Corporation 11

4A COLLIER ON BANKRUPTCY (14th ed. 1971):

¶70.15 7
¶70.28 10

H.R. No. 9142, 93rd Cong., 1st Sess. (1973) 17
Report and Order of Administrative Law Judge, I.C.C. Finance Docket No. 26115, p. 71 11
Treasury Regulations 26 CFR §1.1502-77 ..... 3, 15, 16

Supreme Court of the United States

October Term, 1973
No. _____

ERIE LACKAWANNA RAILWAY COMPANY, Debtor,
Petitioner,

vs.

NORFOLK AND WESTERN RAILWAY COMPANY,
Respondent.

PETITION FOR A WRIT OF CERTIORARI
To the United States Court of Appeals
For the Sixth Circuit

Erie Lackawanna Railway Company respectfully prays that a writ of certiorari issue to review the order of the United States Court of Appeals for the Sixth Circuit entered on September 14, 1973.

OPINIONS BELOW

The Memorandum, Opinion and Order of the United States District Court for the Northern District of Ohio and the Order of the United States Court of Appeals for the Sixth Circuit, neither of which has been reported, appear in the Appendix hereto, *infra*, pp. A1-17.

JURISDICTION

The order of the United States Court of Appeals for the Sixth Circuit vacating the judgment of the District Court was entered on September 14, 1973. This petition for certiorari was filed within 90 days of that date. The jurisdiction of this Court is invoked under 28 U.S.C. Section 1254(1).

QUESTIONS PRESENTED

On June 26, 1972, Erie Lackawanna Railway Company (the "Debtor") filed a Petition for Reorganization under Section 77 of the Bankruptcy Act.

On April 1, 1968, Norfolk and Western Railway Company, through a wholly owned subsidiary, acquired 100% of the common stock of the Debtor pursuant to an order of the Interstate Commerce Commission. During the period from April 1, 1968 through December 31, 1971, the Debtor sustained tax losses of approximately $88,000,000, and generated investment credits of about $3,227,000 on purchases of assets. After Norfolk and Western Railway Company acquired the common stock of the Debtor, it included the Debtor in the making and filing of its consolidated returns with respect to federal income taxes.

In the computation of the Debtor's losses, Norfolk and Western Railway Company made certain tax elections, the effect of which was to reduce substantially the basis of the Debtor's property and to increase its tax losses. In the consolidated returns, Norfolk and Western Railway Company used the tax attributes of the Debtor, its losses and investment credits, to offset its income and to reduce the tax liability of the affiliated group, primarily that of Norfolk and Western Railway Company.

The questions presented are:

1. Whether the tax attributes of Erie Lackawanna Railway Company, namely, its tax losses and investment credits, and the right to exercise tax elections, which Norfolk and Western Railway Company used for its own benefit, are "property" within the meaning of Section 77 of the Bankruptcy Act, title to which vests in the Trustees of the Debtor and over which the District Court has exclusive jurisdiction.

2. Whether the District Court, in order to protect the Debtor's property and prevent its erosion, may exercise its exclusive jurisdiction and control over that property by directing Norfolk and Western Railway Company, when it files a consolidated return that includes the Debtor, that the tax attributes of the Debtor are to be used and tax elections are to be made with respect to the property of the Debtor only as determined by the District Court.

STATUTES AND REGULATIONS INVOLVED

11 U.S.C. Section 205 (Section 77(a) of the Bankruptcy Act) and Section 1502 of the Internal Revenue Code of 1954, and Treas. Reg. Section 1.1502-77 appear in the Appendix hereto, *infra*, pp. A18-20.

STATEMENT OF CASE

On June 26, 1972, Erie Lackawanna Railway Company filed a petition for reorganization under Section 77 of the Bankruptcy Act, which petition was approved by the United States District Court for the Northern District of Ohio. Trustees were appointed on July 31, 1972, and were duly qualified on August 16, 1972.

On April 1, 1968, pursuant to an Order of the Interstate Commerce Commission, Norfolk and Western Railway Company ("N & W") through a subsidiary, Dereco, Inc., acquired 100% of the common stock of the Debtor in exchange for N & W stock with a value of $55,026,000. That Order was approved by this Court in *Penn-Central Merger and N & W Inclusion Cases*, 389 U.S. 486, 525-526 (1968).

For the calendar years 1968 through 1971, N & W has reported its income and that of its affiliates, including the Debtor from April 1, 1968, for federal income tax purposes by filing consolidated returns. In the consolidated returns filed for the years 1968 through 1971, N & W made certain elections, including accelerated methods of depreciation, guideline lives, asset depreciation range system, and amortization of rolling stock, with respect to the depreciable property of the Debtor. As a result of these elections, in the 45 months' period from April 1, 1968 through December 31, 1971, the tax basis of the Debtor's property was eroded by almost $53,700,000 more than it would have if N & W had employed the same methods of depreciation and had made the same elections as the Debtor did prior to its affiliation with N & W.

During the period from April 1, 1968 through December 31, 1971, the Debtor had losses for tax purposes of approximately $88,427,000 which were used by N & W in consolidated returns to offset its taxable income and thereby reduce its tax liability. In addition, the Debtor during that period generated investment credits of approximately $3,227,000, and these credits were utilized to some extent by N & W in further reduction of its tax liability.

On August 3, 1973, the Debtor filed an action for temporary restraining order, preliminary and permanent in-

junctions to restrain N & W from including in its 1972 consolidated return, which was due on September 17, 1973, the losses and credits of the Debtor that were generated after June 26, 1972, (the filing date of the petition for reorganization) and for an accounting and other equitable relief. At the time such action was initiated, the Debtor estimated that on the basis used by N & W in the 1971 return its loss for the entire year ended December 31, 1972 would be $30,000,000, and that for the period from June 27, 1972 through December 31, 1972 the loss would approach $15,000,000, its investment credit would approximate $850,000, and the use by N & W of so-called fast methods of depreciation and amortization would further erode the Debtor's basis of its property by $7,500,000.

On September 10, 1973, the District Court rendered its opinion that the tax attributes of the Debtor were property over which that Court had exclusive jurisdiction. Paragraph 3 of its Order provided:

> "3. N & W be and it is hereby authorized to file on or before September 15, 1973, a consolidated federal income tax return including the income, deductions, and credits of the Debtor and its subsidiaries for the calendar year 1972, prepared in such manner with respect to the Debtor, making such tax elections and taking such deductions and credits which are available to the Debtor as the Trustees, subject to the control of this Court, determine." Appendix, *infra*, p. A15.

The District Court reserved decision and retained jurisdiction to determine the amount of compensation, if any, that N & W is to pay the Debtor for the past, present and future use of the Debtor's tax attributes.

On September 14, 1973, the United States Court of Appeals for the Sixth Circuit vacated the judgment of the

District Court. The Court of Appeals held that the District Court had no authority to control the tax elections affecting the Debtor. The Court of Appeals refused to consider whether the loss and other tax attributes of the Debtor "constitute 'property' vesting in the Trustees under the Bankruptcy Act". Appendix, *infra*, p. A16.

REASONS FOR GRANTING THE WRIT OF CERTIORARI

1. Whether Tax Attributes Constitute "Property" for Bankruptcy Purposes Is an Issue of Crucial Significance in Bankruptcy Administration.

The paramount reason for granting this writ of certiorari is that the issue involved is of crucial significance in bankruptcy administration. The question of statutory interpretation presented—whether tax attributes, namely, net operating losses and investment credits, and the right to exercise tax elections, of a bankrupt are "property" within the meaning of the Bankruptcy Act—is a fundamental one which constantly recurs in bankruptcy administration. Furthermore, the resolution of this issue is one of prime concern to the railroad industry which finds seven major northeastern railroads, including the Debtor, in reorganization proceedings.

a. Tax Attributes Such As Losses and Investment Credits Are Property of Substantial Value That Can Be Realized upon for the Benefit of Creditors.

This Court has previously touched the periphery of the issue. *Segal v. Rochelle*, 382 U.S. 375 (1966). There, the question was whether income tax refunds through loss carrybacks arising out of business losses incurred prior to

bankruptcy were property subject to a turnover order in favor of the trustees. This Court concluded that the tax refund claims were property under Section 70a(5) of the Bankruptcy Act. In reaching that conclusion, this Court stated:

> "The main thrust of §70a(5) is to accrue for creditors everything of value the bankrupt may possess. . . . To this end the term 'property' has been construed most generously and an interest is not outside its reach because it is novel or contingent or because enjoyment must be postponed." *Id.* at 379.

See 4A COLLIER ON BANKRUPTCY ¶70.15, at 137 (14th ed. 1971).

It cannot be denied that the tax losses and investment credits of the Debtor are assets of substantial value and that they can be realized upon for the benefit of creditors. Thus, they play a vital role in achieving the key objective of the Debtor's reorganization proceedings—to secure for creditors every asset of value that the Debtor may possess and to transform the Debtor into a viable and profitable railroad. The value to the Debtor of its tax attributes lies partially in the right to their use by N & W, a profitable, solvent railroad, through consolidated returns as an offset against its taxable income and a direct credit against its tax liability. *See Western Pacific Railroad Corp v. Western Pacific Railroad Co.*, 345 U.S. 247, 276-277 (1952), wherein Justice Jackson in a dissent reaching the merits of the controversy said:

> "We have two affiliated corporations subject to considerable, if not complete, common control, but with different minority interests. One has realized a huge loss the other has enjoyed large net income. If these two can be brought together, a tax saving

amounting in this case to some seventeen million dollars can be made for the profitable company. Congress has authorized, but has not required, that these two be merged by means of a consolidated tax return. Each has the right, but no legal duty, under federal law to join in consolidated returns.

"It may seem anomalous at first glance that a sustained loss can be realized upon as an asset. But it is not the loss; it is the right to use the loss as an offset that is valuable. The market for it is restricted, of course, but this detracts nothing from its value to one in a position to utilize it.

"Each of theses corporations had something to contribute to a tax-saving plan. Either one alone was helpless. But I know of no moral or legal obligation to give away any legal opportunity or advantage just because its owner cannot utilize it himself."

The value of the tax attributes of the Debtor is quickly apparent. For the 45 months' period from April 1, 1968 through December 31, 1971, N & W utilized approximately $88,000,000 of the Debtor's losses as an offset against its own income, a benefit to N & W that in some part rightfully belonged to and must be shared with the Debtor. These losses of the Debtor were created in large measure by the accelerated methods of depreciation elected by N & W which eroded substantially the Debtor's basis for its property. As a result, the Debtor will have a lower tax basis for its assets when it is reorganized than it would have if N & W had adopted tax accounting methods that were for the Debtor's benefit rather than that of N & W. Furthermore, N & W utilized a portion of the Debtor's $3,227,000 of investment credits to reduce its tax liability.

To allow N & W to receive substantial tax benefits arising solely from the Debtor's losses and investment credits, merely because consolidated returns were utilized as a procedural method for reporting income of the affiliated group, unjustly enriches N & W and enables it to use the property of the Debtor to the exclusion of its creditors. *See In re Bob Richards Chrysler-Plymouth Corp., Inc.*, 473 F.2d 262 (2nd Cir. 1973), *cert. denied*, May 29, 1973.

b. Tax Attributes Are Property Within the Meaning of Section 77(a) of the Bankruptcy Act.

Since these tax attributes of the Debtor are so valuable, it is crucial that they be marshalled and conserved for the benefit of the Debtor and its creditors—not N & W, its shareholder. Accordingly, it is incumbent upon the District Court which has jurisdiction over the Debtor to exercise control over and protect these valuable assets. *New Haven Inclusion Cases*, 399 U.S. 392 (1970). That control exists if the Debtor's tax attributes are "property" within the meaning of Section 77(a) of the Bankruptcy Act. The District Court below correctly concluded that the tax attributes were such property over which it exercises exclusive jurisdiction. The Court of Appeals below erred in sidestepping the resolution of that issue.

In *Segal v. Rochelle, supra*, this Court held that loss carryback refund claims arising out of pre-bankruptcy losses are property. *Accord, In re Bob Richards Chrysler-Plymouth Corp., Inc., supra.* It necessarily follows that losses sustained and investment credits generated during bankruptcy likewise fall within the scope of property. The Trustees should have the right to use those tax attributes to the same extent that the Debtor could have but for bankruptcy. *See* Section 6012(b)(3) of the Internal Revenue Code. However, in *Segal*, this Court expressly de-

clined to rule on the question of whether loss carryovers arising from losses sustained in pre-bankruptcy years are to be cloaked with the property label. 382 U.S. at 381. *Case v. New York Central Railroad Company*, 204 N.E.2d 643 (N.Y. Ct. App. 1965) involved an action by minority shareholders of a subsidiary of New York Central to rescind a tax allocation agreement among members of an affiliated group filing consolidated returns. That agreement provided that the profitable corporation must reimburse the loss corporation (Central) for a substantial portion of the taxes which it saved through the use in consolidated returns of Central's losses. In upholding the validity of that allocation agreement the court noted that ". . . the loss shown by Central was under some rather flexible circumstances an asset to Central. It could have been carried forward for seven years . . ." *Id.* at 647.

The issue presented here is complex and unanswered. *See* 4A COLLIER ON BANKRUPTCY ¶70.28, at 398-405 (14th ed. 1971). The time is, therefore, at hand for this Court to decide whether it will attach the property label to losses incurred during bankruptcy which may be carried forward for seven years. Section 172(b) of the Internal Revenue Code of 1954.

c. It Is of Crucial Significance to the Northeast Railroads in Reorganization That Their Tax Attributes Fall Within the Meaning of Property.

This issue of whether tax attributes are property is of importance not only to the Debtor but to other railroads in reorganization. In the ongoing Boston & Maine Railroad reorganization proceedings, the Trustees have taken the position that its operating loss carryovers are a valuable asset of the debtor's estate. Accordingly, it is contending that if its parent, Bomaine Corporation, which in consoli-

dated returns has used the losses of Boston & Maine to offset its income, wishes to continue realizing a benefit from the use of this asset it may do so only if it agrees to compensate Boston & Maine for use of its losses. Report and Order of Administrative Law Judge, I.C.C., Finance Docket No. 26115, p. 71; Bomaine Corporation 1972 Annual Report, p. 19, Note 4.

In the Matter of Lehigh Railroad Company, (E.D. Pa. Bankruptcy No. 70-432) Lehigh, in a situation comparable to that of the Debtor herein, claims that on the filing of its petition for reorganization it ceased to be a member of the affiliated group which included its parent, Penn Central Transportation Company. To protect the value of its asset —its losses—it seeks permission to file amended federal income tax returns on a separate return basis. In the action initiated below in the District Court by the Debtor, it too claimed that when it filed its petition on June 26, 1972 it ceased to be a member of N & W's affiliated group; accordingly, its losses could not be included in the 1972 consolidated return being filed by N & W.

It is apparent that the issue of whether tax attributes are property is not unique to the Debtor. The resolution of that issue by this Court can play a vital role in the reorganization plans of other railroads in reorganization so that their viability can be preserved in the public interest.

d. The Scope of Property with Reference to Tax Attributes Is a Recurring Problem in Bankruptcy Administration and a Conflict Exists in the Circuit Courts of Appeal As to Whether Tax Refunds Arising from Withholding Taxes Is Such Property.

That the scope of "property" within the meaning of the Bankruptcy Act is a recurring problem in bankruptcy administration is readily demonstrable. A conflict exists

between the Ninth and Second Circuits with respect to the question of whether income tax refunds resulting from withholding taxes are property within the meaning of Section 70a(5) of the Bankruptcy Act. In *In re Kingswood*, 343 F. Supp. 498 (C.D. Cal. 1972), *rev'd per curiam*, 470 F.2d 996 (9th Cir. 1973), petition for cert. filed August 13, 1973, (No. 73-289), the District Court held that the refunds were property belonging to the Trustee. The Court of Appeals for the Ninth Circuit reversed and chose to follow the opposite result reached in *In re Cedor*, 337 F. Supp. 1103 (N. D. Cal. 1972), *aff'd per curiam*, 470 F.2d 996 (9th Cir. 1972).

However, *In re Kokoszka*, 479 F.2d 990 (2nd Cir. 1973) is in direct conflict with the *Cedor* result. The Court of Appeals for the Second Circuit held that a tax refund is property passing to a bankruptcy Trustee under Section 70a(5). *In re Jones*, 337 F. Supp. 620 (D.C. Minn. 1971), *leave to appeal denied* (8th Cir. May 14, 1971), *cert. denied*, 404 U.S. 1040 (1972), held that income tax refunds of this nature were property. *See also In re Aveni*, 458 F.2d 972 (6th Cir. 1972), *cert. denied*, 409 U.S. 877 (1972), holding that wages earned prior to bankruptcy are property; *Lines v. Frederick*, 400 U.S. 18 (1970) holding that accrued but unpaid vacation pay was not property.

It is readily apparent that the issue now before this Court—are the losses, investment credits and other tax attributes of the Debtor property within the meaning of Section 77(a) of the Bankruptcy Act—is of significant immediate concern and importance involving millions of dollars that needs resolution by this Court. Furthermore, the recurring litigation involving the scope of "property" illustrates the need for the Supreme Court to give its authoritative answer to the question of whether tax attributes are such property.

2. Whether the District Court in Fulfilling Its Duty to Protect the Property of the Debtor, Including Its Tax Attributes, Can Direct the Parent As to What Tax Elections Are to Be Made in a Consolidated Return Which Affect the Debtor's Property Is a novel and Important Issue in the Administration of the Consolidated Returns Regulations.

This case involves the novel issue of whether the District Court can, in the exercise of its exclusive jurisdiction over the Debtor and its property, control tax elections, such as accelerated depreciation, asset depreciation range system and amortization of rolling stock, which directly affect that property when consolidated returns are filed that include the Debtor. The District Court below determined that the tax elections made by N & W substantially eroded—to the extent of about $53,700,000 through 1971—the tax basis of the Debtor's property as a result of which the Debtor could suffer irreparable damage. The District Court stated that such erosion could "critically affect the Trustees' ability to devise an acceptable and successful plan of reorganization." Appendix, *infra*, p. A8.

The course of action pursued by N & W of maximizing the depreciation and amortization deductions with respect to the Debtor's property served to increase its tax losses, all of which redounded to the benefit of N & W through the offset of those losses against its own income. The District Court properly determined that in view of the conflicting position in which N & W found itself the responsibility for determining what tax elections are to be made rested with the District Court.

> "Thus, the paradox of the dilemma confronting N & W is self-evident. To serve its own best corporate interests, it must, of necessity, elect a course of action

injurious to the Debtor. Conversely, to accede to the wishes of the Trustees would be prejudicial to its own best business interest. Under the existing circumstances, no stigma is intended against N & W for pursuing accepted, good business dictates in selecting the course most beneficial to its own position even though the ultimate consequence of its action may, in some degree, irreparably injure the property of the Debtor.

"Conscientious adherence to the Congressional mandate imposed upon the Court to protect and conserve the property of the Debtor permits no recourse but to relieve N & W of its burdensome conflict in discharging its fiduciary responsibilities." Appendix, *infra*, p. A10.

The Court of Appeals summarily disposed of the issue of who has the right to control the tax elections on the erroneous basis that it could find no authority for a court to order what income or deductions to include in a tax return. It could find none because of the uniqueness of the issue—a parent and an insolvent subsidiary in conflicting positions, the former doing everything to maximize the losses of the Debtor subsidiary through the utilization of accelerated methods of depreciation, and the latter striving to minimize its losses through the utilization of conservative methods of depreciation. The correct resolution of that issue was reached by the District Court. The District Court found, and the Court of Appeals below overlooked this finding, that the tax elections made by N & W affect the Debtor's property. Therefore, it was incumbent upon the District Court in protecting that property to relieve N & W of its responsibility for making those elections. The consolidated returns regulations do not compel a different result.

It is true that N & W, as the common parent of the affiliated group, is designated in the consolidated returns regulations as the agent for the Debtor, but that authority is confined to N & W's dealings with the Treasury and Internal Revenue Service in matters relating to the consolidated tax liability. Regs. Sec. 1.1502-77(a). The obvious purpose of the regulation's designating the parent as the representative for all members of the affiliated group is procedural and solely a matter of convenience in the administration of the tax laws. That regulatory provision is not intended to, nor does it, create legal rights between the Debtor and N & W in their relationship with one another.

That this analysis of the relationship between the Debtor and N & W is correct is buttressed by the recent decision of the Court of Appeals for the Second Circuit, *In re Bob Richards Chrysler-Plymouth Corp., Inc., supra.* There, the dispute was over which corporation in an affiliated group was entitled to an income tax refund—the bankrupt which had the earnings or the parent corporation to which the refund check had been sent. Relying on *Segal v. Rochelle, supra,* the Court held that the bankrupt was entitled to the refund. The Court made the following comments with respect to the parent's position as agent for the subsidiary under the consolidated return regulations.

> "The only reason for the tax refunds not being paid directly to the subsidiary is because income tax regulations require that the parent act as the sole agent, when duly authorized by the subsidiary, to handle all matters relating to the tax return. Accordingly, the refund is made payable to the parent and the acceptance of the refund by the parent discharges any liability of the government to any subsidiary. But these regulations are basically procedural in purpose

and were adopted solely for the convenience and protection of the federal government." 473 F.2d at 265.

Accordingly, the answer to the question of whether the Debtor or N & W controls the tax elections affecting the Debtor's property is not found in the consolidated returns regulations. The answer depends on whether tax attributes are property. If they are, then Section 77(a) of the Bankruptcy Act vests in the District Court exclusive jurisdiction over that "property". This Court in *Segal* has stated that the definition of "property" is to be determined in the light of the purposes of the Bankruptcy Act. 382 U.S. at 379. The purposes of that Act obviously differ from those of the consolidated returns regulations under the Internal Revenue Code. The main thrust of Section 77(a) of the Bankruptcy Act is to secure for creditors all assets of the Debtor, and to transform it into a living, sound railroad for the benefit of the public, whereas Regs. Sec. 1.1502-77 are merely procedural in purpose to protect the government against having to deal with a multiplicity of parties. The purposes of the Bankruptcy Act must prevail over those of the consolidated returns regulations. Accordingly, since the tax elections vitally affect the Debtor's property, the right to exercise those elections must rest solely with the District Court.

The Court of Appeals failed completely to grasp the point at issue: Who should exercise control and jurisdiction over the property of the Debtor, the District Court which is charged with the responsibility of obtaining and conserving every asset of the Debtor whether minimal or contingent, or N & W whose selfish interests compelled it to a course of action that eroded the Debtor's property and maximized the Debtor's loss, all to the benefit of N & W to the extent of at least $88,000,000? The mere statement of the question quickly dictates the answer—the District

Court should exercise control over the property of the Debtor, because the contrary response would deprive the District Court of that jurisdiction and control over the Debtor's property which the Bankruptcy Act confers only upon it.

It is apparent that a crucial aspect of the Debtor's chances of being metamorphosed into a viable, profitable railroad depends upon the ability of the District Court to determine what use is to be made of its tax attributes. Substantial efforts are being expended by Congress and the Administration to resolve the plight of the bankrupt northeast railroads. In furtherance of these efforts, on November 8, 1973, the House of Representatives passed a Bill, known as the "Regional Rail Reorganization Act of 1973", which has as one of its purposes and effects the reorganization of the ailing northeast railroads into an economically viable rail system. H.R. 9142, 93rd Cong., 1st Sess. (1973). If this Bill, or one of similar effect, is enacted, the significance of minimizing now the depreciation deductions of the Debtor and thus reducing its losses becomes apparent. The erosion of the Debtor's tax basis would be preserved to the point where depreciation deductions would be available as an offset against income in subsequent profitable years. Such a course of action would inure to the benefit of the creditors of the Debtor and the general public, which is where that benefit rightfully belongs.

The Court of Appeals committed grievous error in failing to determine that the Debtor's tax elections should be exercised by the District Court, thereby erroneously placing the responsibility for exercising tax elections involving the Debtor's property in the hands of N & W which has utilized the Debtor's tax attributes for its own substantial benefit to the exclusion of the Debtor and its creditors and contrary to the public interest.

CONCLUSION

For these reasons a writ of certiorari should issue to review the order of the Court of Appeals for the Sixth Circuit.

Respectfully submitted,

SHERMAN DYE
RICHARD KATCHER
1956 Union Commerce Building
Cleveland, Ohio 44115
Counsel for Petitioner

APPENDIX

OPINION AND ORDER OF THE DISTRICT COURT

(Filed September 10, 1973)

THE UNITED STATES DISTRICT COURT
THE NORTHERN DISTRICT OF OHIO
EASTERN DIVISION

In Proceedings for the Reorganization of a Railroad
No. B72-2838

IN THE MATTER OF
ERIE LACKAWANNA RAILWAY COMPANY
Debtor

MEMORANDUM, OPINION and ORDER NO. 147

KRUPANSKY, *J.*

This is an action initiated by the Trustees of Erie Lackawanna Railway Company (Erie) for a permanent injunction restraining the Norfolk and Western Railway Company (N & W) from filing any federal, state, or local consolidated, combined, or joint tax returns including the income, deductions and credits of the Debtor, Erie, for any period subsequent to June 26, 1972, together with an accounting and other equitable relief.

On June 26, 1972, the Debtor, Erie, filed a petition for reorganization under Section 77 of the Bankruptcy Act, which petition was approved by this Court in Order No. 1 vesting exclusive jurisdiction over the Debtor and its property in this Court. Trustees were appointed on July 31, 1972, and were duly qualified on August 16, 1972. All title

to property including the rights, privileges, powers and duties to operate and manage the Debtor's business and properties were, on that date, vested in the Trustees subject to the control of this Court. 11 U.S.C. §205, as amended.

In this action, it is asserted by the Trustees that tax losses, investment credits, and all other tax attributes of the Debtor and the right to their exercise and use are property rights of the Debtor, title to which is vested in the Trustees subject to the exclusive jurisdiction of this Court.

Introductory to the issues here in controversy, the following summary leading to the adversary position of the parties is essential for a basic understanding requisite to a final determination.

The Norfolk and Western system acquired ownership of 100% of the voting stock of Erie on April 1, 1968, pursuant to an Order of the Interstate Commerce Commission which followed lengthy proceedings initiated by Erie with a Petition for Inclusion before said Commission seeking to order N & W to include Erie in its system. The N & W resisted the order charging that Erie was at best a marginal railroad with no reasonable prospect of long-range profitable operations.

In support of its Petition for Inclusion, Erie successfully maintained that N & W would realize a net tax savings of approximately $1,000,000 annually after inclusion through use of tax investment credits generated by Erie, together with other tax deductions which would virtually insure the investment in Erie which N & W would be required to make under the plan for inclusion.

By order of the ICC dated January 9, 1967, N & W was compelled to acquire Erie's stock. N & W exercized its right of appeal, however, the ICC order was ultimately sus-

tained by the Supreme Court of the United States on January 15, 1968. *Penn-Central Merger and N & W Inclusion Cases,* 389 U.S. 486 (1968). Pursuant to approval by the ICC, acquisition of all of Erie's voting stock by N & W was accomplished by and through its totally owned subsidiary, Dereco, thus permitting N & W to completely insulate itself from the accrued indebtedness and future liabilities of Erie, but retaining wide flexibility to utilize all advantages collateral to the inclusion of Erie in its system.

Thereafter, Erie had a substantial deficit in each of the years from 1968 to 1972.

N & W has filed consolidated tax returns for its system lines since 1954. When Erie became part of this system, N & W was required by Section 1502 of the Internal Revenue Code and the regulations thereunder to include Erie in its consolidated return. By virtue thereof, N & W made the available elections which reduced consolidated tax liability, including accelerated methods of depreciation, guideline lives, the asset depreciation range system, and amortization of rolling stock in determining the net income or loss of Erie for consolidated tax return purposes. These are the elections which the N & W used for itself and other members of the N & W system. As a result of N & W's use of these tax accounting methods and the large losses suffered by the Erie since its acquisition, the N & W has received substantial tax benefits from its right to include Erie in its consolidated return.

The ratio between N & W's actual dollar investment in Erie, to date, and the substantial tax benefits received resulting from the ICC inclusion order is not clearly reflected by the evidence before the Court. Whatever that ratio proves to be, it must be received and considered within the context of Section 77 of the Bankruptcy Act.

Undeniably, the ultimate objective of a reorganization proceeding is the metamorphosis of a debt-ridden, unprofitable railroad into a dynamic, viable company capable of serving the general public in the interests of both the national economy and defense.

To accomplish this transition, it is necessary to reduce or liquidate indebtedness incurred during years of unprofitable operation. This task, inherent in all reorganization proceedings, is neither simple nor pleasant, for success dictates that creditors, secured and general, stockholders, and the public must stand ready to assume a share of the burden, so that a viable enterprise may emerge from the proceedings for the benefit of all. Thus, N & W cannot claim preferential treatment and must stand with the public and the creditors and await the outcome of the reorganization with optimism.

The broad scope of authority vested in a Reorganization Court by Congressional enactment of Section 77 of the Bankruptcy Act is explicitly defined by the pronouncements of the Supreme Court in the *New Haven Inclusion Cases,* 399 U.S. 392, 420, (1970) where it stated:

> The jurisdiction of the reorganization court was not open to question. Upon its approval of the New Haven's petition for reorganization in 1961, that court had acquired "exclusive jurisdiction of the debtor and its property wherever located * * *." Bankruptcy Act, §77 (a), 11 U.S.C. §205 (a). Subject to the court's control, the trustees whom it appointed were empowered "to operate the business of the debtor." Id., §77 (c) (2), 11 U.S.C. §205 (c) (2). They were thus charged with the dual responsibility of conserving the debtor's estate for the benefit of creditors and preserving an ongoing railroad in the public interest. Massachusetts v. Bartlett, 384 F. 2d 819, 821, cert. denied, 390 U.S.

1003, 88 S.Ct. 1245, 20 L. Ed. 2d 103; 5 Collier on Bankruptcy ¶77.02, at 469-470 (14th ed. 1969). With these goals in view, the statute bestowed a "broad and general" authority upon both the court and the trustees. Cf. Palmer v. Massachusetts, 308 U.S. 79, 85, 60 S.Ct. 34, 37, 84 L. Ed. 93. The provisions of §77 "doubtless suffice[d] to confer upon the [reorganization court] power appropriate for adjusting property rights in the railroad debtor's estate and, as to such rights, beyond that in ordinary bankruptcy proceedings." Id., at 85-86, 60 S.Ct., at 37; Cf. 5 Collier, supra, ¶77.11, at 498-499.

Apparent from the foregoing, on June 26, 1972, when the petition for reorganization was filed by Erie, the Court's jurisdiction vested to adjudicate controversies relating to all property in the actual or constructive possession of the Debtor. *Thompson v. Magnolia Petroleum Co.*, 309 U.S. 478 (1940).

It necessarily follows that an affirmative finding by the Court that Debtor's tax attributes constitute "property" within the intent and meaning of Section 77 would bring such property within the orbit of the Court's exclusive jurisdiction.

Tax losses have been consistently recognized as assets of definitive value as emphasized by the language of Mr. Justice Jackson's dissent in *Western Pacific Railroad Corp. v. Western Pacific Railroad Co.*, 345 U.S. 247, 273 (1956).

Electing to comment upon the merits of the controversy rather than the procedural aspects considered by the majority of the Court in disposing of the case, Justice Jackson pragmatically characterized tax losses as assets of value for which compensation could be realized, a concept long recognized in commercial circles.

"We have two affiliated corporations subject to considerable, if not complete, common control, but with different minority interests. One has realized a huge loss; the other has enjoyed large net income. If these two can be brought together, a tax saving amounting in this case to some seventeen million dollars can be made for the profitable company. Congress has authorized, but has not required, that these two be merged by means of a consolidated tax return. Each has the right, but no legal duty, under federal law to join in consolidated returns.

It may seem anomalous at first glance that a sustained loss can be realized upon as an asset. But it is not the loss; it is the right to use the loss as an offset that is valuable. The market for it is restricted, of course, but this detracts nothing from its value to one in a position to utilize it.

Each of these corporations had something to contribute to a tax-saving plan. Either one alone was helpless. But I know of no moral or legal obligation to give away any legal opportunity or advantage just because its owner cannot utilize it himself.

* * *

On the face of it, the conclusion would seem warranted that the plaintiff is entitled to what fair arm's-length bargaining would probably have yielded. To ask this can hardly be stigmatized as capitalizing mere nuisance value. This is not the blackmailing transaction which offers to forego doing another injury if bought off. This merely seeks a share in the benefit which it transferred."

Western Pacific Railroad Corp. v. Western Pacific Railroad Co., supra 276, 277.

The Supreme Court in 1966 recognized that the term "property" as used in Section 70(a)(5) of the Bankruptcy Act must be construed "most generously" and that a tax loss carryback is not outside the reach of the Bankruptcy Court merely ". . . because it is novel or contingent or because enjoyment must be postponed." *Segal v. Rochelle*, 382 U.S. 375 (1966) at 379. Accord, *Danielson v. United States*, 416 F. 2d 408, 410 (9th Cir., 1969); *In Re Treguboff*, 305 F. Supp. 1013, 1016, 1017 (C.D. Calif. 1968); *Kennedy v. Powell*, 366 F. 2d 346, 348 (9th Cir., 1966), *cert. denied*, 368 U.S. 910 (1966). See also *Case v. New York Central Railroad Company*, 204 N.E. 2d 643, 647 (N.Y. Ct. App. 1965), where it was recognized that ". . . the loss shown by Central was under some rather flexible circumstances an asset to Central. It could have been carried forward for seven years. . ."

Contrary to the position of Norfolk and Western, *In re Scranton Corp.*, 235 F. Supp. 770 (M.D. Pa. 1964), also supports the proposition that the right to make a tax loss available to another corporation through a consolidated return is a property right. The *Scranton* court recognized jurisdiction over the subject matter of the Tax Court litigation but like this Court, found it unnecessary to enjoin Tax Court proceedings to protect the property of the Debtor. See also *In re Penn Central Transportation Company*, 453 F. 2d 520 (3rd Cir. 1972).

In light of the foregoing authority, the Court concludes that tax losses are property within the intent and meaning of Section 77 of the Bankruptcy Act over which the Court may, within its discretion, exercise exclusive summary jurisdiction.

Similarly, tax elections as to the methods of depreciation and amortization which are to be taken by N & W affect the property of the Debtor which it is the duty of

the Trustees and this Court to protect. At the hearing, Trustees introduced a comparative analysis between the deduction claimed by N & W with respect to Erie property in consolidated returns from April 1, 1968 through December 31, 1971 with the deductions which would have been taken under the depreciation methods and procedures used by Erie prior to affiliation. For the forty-five month period, the excess claimed by N & W on the so-called fast write-off methods approached $53,700,000. The Trustees estimate that the difference in depreciation deductions for the full year 1972 would approximate $15,200,000, of which approximately $7,500,000 would relate to the period between June 26 and December 31, 1972.

In Rev. Rul. 68-48, 1968-1 Cum. Bull. 301, 303, the Internal Revenue Service ruled that "[a] trustee in bankruptcy must use the bankrupt's adjusted basis when computing gain or loss on the sale of assets for the benefit of the estate in bankruptcy." Under Section 167 (g), "[t]he basis on which exhaustion wear and tear . . . are to be allowed . . . shall be the adjusted basis provided in Section 1101 . . . ." Thus, the Debtor would have a lower basis on which to compute gain or loss from the sale of assets and to compute further depreciation should Norfolk and Western be permitted to continue to exercise the Debtor's tax elections.

Clearly this substantial erosion of the tax basis of the Debtor's property will result in irreparable damage and critically affect the Trustees' ability to devise an acceptable and successful plan of reorganization.

The fact that the debtor cannot presently use either its tax losses or the increased basis of its assets does not diminish the obligation and duty of this Court to protect all of the property and rights of the bankrupt whether these be contingent or inchoate. *Segal v. Rochelle, supra.*

N & W's assertion that the Debtor cannot profitably use its tax attributes now or in the immediate future does not divest this Court of jurisdiction over such property.

Erie's investment credits like its tax losses come within the same property classification subject to the Court's jurisdiction.

The reorganization court sitting in equity would be remiss to foreclose the only forum available to the Trustees to protect and preserve the Debtor's property rights. That the Trustees have no adequate remedy at law is demonstrated by an analysis of applicable statutory enactments and treasury regulations.

Treasury Regulations Sections 1.1502.75; 1.1502.77, promulgated pursuant to 26 U.S.C. Section 1502 effectively:

1. Preclude the Trustees from applying to the Commissioner for permission to withdraw from the affiliated group;
2. Preclude the Trustees from representing the Debtor's interests in any proceeding related to tax liability, elections etc. before either the Commissioner of Internal Revenue or the Tax Court of the United States; and
3. Require the Trustees to recognize and rely upon its parent N & W as its agent in all matters before the aforementioned tribunals.

Stripped of authority to either initiate or pursue any action for relief before the only available forums expressly created by statute to afford relief, the Trustees must, of necessity, resort to the reorganization court to implement its statutory duty to protect the Debtor's property.

Of equal concern to the Court is the apparent conflict of interest impressed upon N & W by the reorganization proceedings.

N & W as parent-agent of the affiliated group, invested with plenary authority to determine without recourse the use of Erie's property for tax purposes was free to exercise such privilege so long as a common interest, free of conflict, prevailed between parent and subsidiary.

The impact of the intervening reorganization condemned the relationship to one of irreconcilable conflict.

Thus, the paradox of the dilemma confronting N & W is self-evident. To serve its own best corporate interests, it must, of necessity, elect a course of action injurious to the Debtor. Conversely, to accede to the wishes of the Trustees would be prejudicial to its own best business interest. Under the existing circumstances, no stigma is intended against N & W for pursuing accepted, good business dictates in selecting the course most beneficial to its own position even though the ultimate consequence of its action may, in some degree, irreparably injure the property of the Debtor.

Conscientious adherence to the Congressional mandate imposed upon the Court to protect and conserve the property of the Debtor permits no recourse but to relieve N & W of its burdensome conflict in discharging its fiduciary responsibilities.

The existence of exclusive summary jurisdiction over all property in the actual or constructive possession of the Debtor, including matters involving such property before the Commissioner of Internal Revenue or the Tax Court, does not mean that the reorganization court must necessarily assert its jurisdiction and restrain another forum with concurrent jurisdiction over the same matter from

proceeding. This is true whether the other forum be a state or federal court in the judicial branch of government, or an administrative body in the executive branch. *Thompson v. Magnolia Petroleum Co., supra*; *In Re Scranton Corporation, supra.*

The fundamental basis for restraining an action outside the reorganization court is that such action could unduly hinder, delay, burden, interfere, or be inconsistent with the pending corporate reorganization. In the case at bar, the Court makes no such finding. The Court defers to the Commissioner of Internal Revenue or the Tax Court for a determination of the issue of the validity of the existing affiliation between N & W and Erie for purpose of filing consolidated income tax returns.

To Summarize, the Court finds:

1. Tax attributes of the Debtor, including without limitation the right to exercise elections and take deductions and credits permitted under the Internal Revenue Code and the regulations issued thereunder, are property of the Debtor over which this Court has jurisdiction.

2. The choice of tax elections affects the tax basis of the Debtor's property and the future deductions which may be taken with respect to such property.

3. Some, if not all, of the tax elections which are available to the Debtor cannot be reversed or revoked once made.

4. The Debtor and its creditors will suffer irreparable injury if N & W is permitted to continue to make such tax elections and to take such deductions and credits which are available to the Debtor as N & W has made and taken in the past and as it intends to continue to make and take in the future.

5. The Debtor has no adequate remedy at law.

Accordingly, It Is Ordered:

1. The preliminary injunction heretofore issued is dissolved.

2. N & W and its directors, officers, employees, and agents be and they are hereby permanently enjoined from exercising or making any and all tax elections and from taking any and all deductions and credits which are available to the Debtor in the computation of its separate taxable income under the Internal Revenue Code and the regulations thereunder, except such tax elections, deductions, and credits as the Trustees, subject to the control of this Court, shall determine.

3. N & W be and it is hereby authorized to file on or before September 15, 1973 a consolidated federal income tax return including the income, deductions, and credits of the Debtor and its subsidiaries for the calendar year 1972, prepared in such manner with respect to the Debtor, making such tax elections and taking such deductions and credits which are available to the Debtor as the Trustees, subject to the control of this Court, determine.

4. The Trustees be and they hereby are authorized and directed to file on or before September 15, 1973 an income tax return for the Debtor and its subsidiaries for the period commencing June 27, 1972 and ending on December 31, 1972, prepared in such manner, making such tax elections and taking such deductions and credits as the Trustees shall determine.

5. N & W be and it is hereby directed and ordered to supply copies of all consolidated, combined, or joint tax returns, whether federal, state or local, which have been,

or may hereafter be, filed by N & W and which include the Debtor and to inform the Trustees in writing of all tax elections made and investment credits taken on such returns and the manner of preparation of such returns.

6. N & W be and it is hereby directed and ordered to advise the Trustees of all tax audits, tax proceedings, and other tax matters affecting the Debtor.

7. That this Court shall reserve decision and retain jurisdiction:

a. To determine the amount of compensation, if any, that N & W shall pay the Debtor for the past, present, or future use of the Debtor's tax attributes.

b. To determine all other issues raised by the Trustees' Application.

IT IS SO ORDERED.

/s/ ROBERT P. KRUPANSKY
United States District Judge

Dated: September 10, 1973

ORDER OF THE COURT OF APPEALS

(Filed September 14, 1973)

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

IN THE MATTER OF
ERIE LACKAWANNA RAILWAY COMPANY
Debtor

ORDER

Before: WEICK, CELEBREZZE and PECK, *Circuit Judges.*

Norfolk and Western Railway Company (N & W) has appealed to this Court from a permanent injunction against it entered in the reorganization proceeding of its wholly owned subsidiary, Erie Lackawanna Railway Company (Erie), Debtor, pending in the District Court under Section 77 of the Bankruptcy Act.

N & W is required by law to file its consolidated income tax return on or before September 17, 1973. In a summary proceeding in the District Court the Trustees for Erie challenged the right of N & W in its consolidated income tax return (not yet filed) to use losses and investment credits of Erie. The District Judge granted temporary and preliminary injunctions against N & W restraining it from so doing, and finally on September 10, 1973, granted the permanent injunction.

We granted an expedited appeal, convened a panel in Cleveland, Ohio, to hear oral arguments, and read the briefs of counsel, although this Court was in recess.

The pertinent provisions of the permanent injunction are as follows:

> "2. N & W and its directors, officers, employees, and agents be and they are hereby permanently enjoined from exercising or making any and all tax elections and from taking any and all deductions and credits which are available to the Debtor in the computation of its separate taxable income under the Internal Revenue Code and the regulations thereunder, except such tax elections, deductions, and credits as the Trustees, subject to the control of this Court, shall determine.
>
> "3. N & W be and it is hereby authorized to file on or before September 15, 1973 a consolidated federal income tax return including the income, deductions, and credits of the Debtor and its subsidiaries for the calendar year 1972, prepared in such manner with respect to the Debtor, making such tax elections and taking such deductions and credits which are available to the Debtor as the Trustees, subject to the control of this Court, determine."

N & W had been forced to acquire the controlling stock of Erie by order of the Interstate Commerce Commission (ICC), entered in an inclusion proceeding on April 1, 1968. These proceedings were instigated by Erie. The decision of ICC was affirmed by a three-Judge District Court in *Erie Lackawanna Ry. v. United States*, 279 F. Supp. 316, 346 (S.D. N.Y. 1967), and by the Supreme Court in *Penn. Central Merger Cases*, 389 U.S. 486, 525, 526 (1968). The price fixed by ICC for the exchange of stock was shares of N & W stock worth about $55,000,000.

The principal argument of Erie in these proceedings and before the Courts was that as a result of the merger N & W would realize large tax benefits. ICC stated:

"Even if EL earnings are not sufficient to support the proposed stock exchange ratios, N & W's investment in EL would be protected by [the] substantial tax benefits [described in the EL testimony]." (330 ICC at 846.)

Under applicable statutes and regulations N & W has been filing consolidated income tax returns since 1954. Upon its forced acquisition of all the common capital shares of Erie in 1968, N & W has since included in its consolidated tax return the income or losses and other tax attributes of Erie. It cannot now change without the consent of the Commissioner of Internal Revenue, who will undoubtedly audit these returns.

We can find no authority for a District Court, prior to the preparation and filing of a tax return to mandatorily order a taxpayer what income or deductions to include therein. The District Court seemed to recognize this thesis when it stated in its opinion:

"The fundamental basis for restraining an action outside the reorganization court is that such action could unduly hinder, delay, burden, interfere, or be inconsistent with the pending corporate reorganization. In the case at bar, the Court makes no such finding. The Court defers to the Commissioner of Internal Revenue or the Tax Court for a determination of the issue of the validity of the existing affiliation between N & W and Erie for purpose of filing consolidated income tax returns."

Other substantial issues in the case are whether the loss and other tax attributes of Erie constitute "property" vesting in the Trustees under the Bankruptcy Act. If property, did N & W acquire such rights under the hold-

ings of ICC and the Courts upholding the merger because such rights were available to N & W?

We are of the opinion that these issues were prematurely determined by the District Court.

We are of the further opinion that the Trustees have an adequate remedy at law, for in its opinion the District Court stated:

> "7. That this Court shall reserve decision and retain jurisdiction:
>
> "a. To determine the amount of compensation, if any, that N & W shall pay the Debtor for the past, present, or future use of the Debtor's tax attributes.
>
> "b. To determine all other issues raised by the Trustees' Application."

Thus, the question of whether the past, present or future tax attributes belong to Erie or N & W can later be determined by the District Court in the event that such issues are not adjudicated administratively by the Commissioner, the Tax Court or on appeal to a United States Court of Appeals.

It is therefore ORDERED that the judgment of the District Court be vacated; that the Trustees and N & W may file their own tax returns, in which they may include their income or deductions, the validity of which is subject to later determination administratively or by the Courts.

Entered by Order of the Court
/s/ JAMES A. HIGGINS
Clerk

BANKRUPTCY ACT, 11 U.S.C. §205

§ 205. Reorganization of railroads engaged in interstate commerce—Petition for reorganization by railroad, subsidiary or creditors; venue; proceedings thereon; jurisdiction of court over debtor and property

(a) Any railroad corporation may file a petition stating that it is insolvent or unable to meet its debts as they mature and that it desires to effect a plan of reorganization. The petition shall be filed with the court in whose territorial jurisdiction such corporation, during the preceding six months or the greater portion thereof, has had its principal executive or operating office, and a copy of the petition shall at the same time be filed with the Interstate Commerce Commission (hereinafter called the "Commission"): *Provided,* That when any railroad, although engaged in interstate commerce, lies wholly within one State, such proceedings shall be brought in the Federal district court of the district in which its principal operating office in such State during the preceding six months or the greater portion thereof has been located. The petition shall be accompanied by payment to the clerk of a filing fee of $100, which shall be in addition to the fees required to be collected by the clerk under other sections of this title. Upon the filing of such a petition, the judge shall enter an order either approving it as properly filed under this section, if satisfied that such petition complies with this section and has been filed in good faith, or dismissing it, if he is not so satisfied. If the petition is so approved, the court in which such order is entered shall, during the pendency of the proceedings under this section and for the purposes thereof, have exclusive jurisdic-

tion of the debtor and its property wherever located, and shall have and may exercise in addition to the powers conferred by this section all the powers, not inconsistent with this section, which a Federal court would have had if it had appointed a receiver in equity of the property of the debtor for any purpose.

* * * * *

INTERNAL REVENUE CODE OF 1954, 26 U.S.C. §1502

Sec. 1502. Regulations.

The Secretary or his delegate shall prescribe such regulations as he may deem necessary in order that the tax liability of any affiliated group of corporations making a consolidated return and of each corporation in the group, both during and after the period of affiliation, may be returned, determined, computed, assessed, collected, and adjusted, in such manner as clearly to reflect the income tax liability and the various factors necessary for the determination of such liability, and in order to prevent avoidance of such tax liability.

TREASURY REGULATIONS, 26 CFR §1.1502-77

§ 1.1502-77. Common parent agent for subsidiaries.

(a) *Scope of agency of common parent corporation.* The common parent, for all purposes other than the making of the consent required by paragraph (a) (1) of § 1.1502-75, shall be the sole agent for each subsidiary in the group,

duly authorized to act in its own name in all matters relating to the tax liability for the consolidated return year. No subsidiary shall have authority to act for or to represent itself in any such matter. For example, any election available to a subsidiary corporation in the computation of its separate taxable income must be made by the common parent, as must any change in an election previously made by the subsidiary corporation; all correspondence will be carried on directly with the common parent; the common parent shall file for all extensions of time including extensions of time for payment of tax under section 6164; notices of deficiencies will be mailed only to the common parent, and the mailing to the common parent shall be considered as a mailing to each subsidiary in the group; notice and demand for payment of taxes will be given only to the common parent and such notice and demand will be considered as a notice and demand to each subsidiary; the common parent will file petitions and conduct proceedings before the Tax Court of the United States, and any such petition shall be considered as also having been filed by each such subsidiary. The common parent will file claims for refund or credit, and any refund will be made directly to and in the name of the common parent and will discharge any liability of the Government in respect thereof to any such subsidiary; and the common parent in its name will give waivers, give bonds, and execute closing agreements, offers in compromise, and all other documents, and any waiver or bond so given, or agreement, offer in compromise, or any other document so executed, shall be considered as having also been given or executed by each such subsidiary.